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SUBJECT: UKRAINE: CHANCES FOR OPIC'S RETURN FADE AS GOU ADDS NEW
CONDITIONS

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Summary and Comment

1. (SBU) The chances of OPIC returning to Ukraine soon have faded after the GOU introduced new requirements into the proposed settlement. For over a year, OPIC has been negotiating with Tasko Corp., a private firm that the GOU designated to settle the outstanding OPIC claim on its behalf, and late last year a solution appeared imminent. In December the GOU changed course, however, and said it must conduct a tender to select a company, and not necessarily Tasko, to settle the claim with OPIC. This surprising announcement came shortly after OPIC and Tasko reached full agreement on the modalities of the settlement, and the USG and GOU publicly signed an MOU laying out the path for OPIC's return. The GOU made overall progress in the bilateral discussions contingent upon OPIC and Tasko reaching an understanding, but now nobody in the GOU will explain this about-face. While open tenders are generally a good thing, it is now unclear how long the tender will delay OPIC's return, and it could derail the proposed solution completely. The GOU's actions may reflect continued deep-seated opposition to a settlement within the GOU, and/or an attempt by Tasko's competitors to wrest the deal away. PM Tymoshenko and Deputy PM Nemyrya have repeatedly told the USG that OPIC's return is a top priority, and earlier this week Nemyrya promised to get an agreement in time for a trip to Washington in the next week. Yet the latest actions cast doubt on their willingness to take the steps necessary to remove this irritant from the bilateral relationship. End summary.

Background: The Long Road to a Solution

2. (SBU) OPIC has been closed for business in Ukraine since the GOU failed to reimburse OPIC for an expropriation claim dating from the late 1990s. OPIC had insured Alliant Kyiv, a Ukrainian joint venture of U.S. firm Alliant Techsystems, that intended to disassemble and recycle Soviet-era munitions with Ukrainian partners. OPIC paid out a \$17.7 million claim to Alliant Techsystems after the joint venture was expropriated by the GOU. In accordance with the 1992 intergovernmental agreement that provides for OPIC's operations in Ukraine, OPIC turned to the GOU for compensation. The GOU has steadfastly refused to acknowledge the claim and or pay any compensation. Successive GOUs expressed interest in a no-fault solution, because OPIC's absence was keeping needed U.S. investment away while harming Ukraine's image as an investment destination. In the ensuing years several attempts to find a no-fault solution failed on account of successive governments' inability, or unwillingness, to back them.

GOU Suggests a Company - Tasko - To Settle the Claim

13. (SBU) In the autumn of 2007, the then Yanukovych government suggested a new solution to the USG that OPIC quickly supported. The GOU designated a company - Tasko Corp. - to settle the claim on its behalf. The GOU would grant Tasko, a small private munitions company run by a respected former Deputy Minister of Industrial Policy, a license to recycle and export small caliber munitions. Tasko would use revenues generated from the business to pay OPIC over a number of years. A commercial basis for the payment was needed, since Ukrainian law prevented Tasko from simply wiring money to OPIC without receiving anything in return. Hence it was agreed that Tasko purchase the equity and other interests in the defunct Alliant Kyiv, which Alliant Techsystems had assigned to OPIC as part of the settlement of the insurance claim. OPIC would acknowledge the payment as settlement for its claim against the GOU. It would reopen in Ukraine upon receipt of the first payment, and upon receipt of a firm guarantee that Tasko would make the subsequent payments in a timely manner. The solution worked for all sides: in OPIC's view, Tasko was a vehicle used by the GOU to pay the claim, and it did not take any commercial risk in the transaction, since the GOU and Tasko agreed to secure the payments by a viable insurance policy or bank guarantee. In the GOU's view it was not admitting fault, since not it, but a private company, was paying OPIC.

14. (SBU) Negotiations continued seamlessly after the Tymoshenko government came to power in late 2007. Economy Minister Danylyshyn was tasked with the issue, and Deputy Minister Viktor Panteyelenko chaired a vast interagency working group which met with Embassy regularly throughout 2008. From the outset, Tasko's President Valeriy Pavlyukov and his main deputies participated in the meetings, and began direct negotiations with OPIC in the summer. In late October agreement was reached: Tasko would pay OPIC \$5 million

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in equal installments over ten years without interest, and the state-owned Ukreximbank or another satisfactory guarantor would guarantee the deal.

GOU Ducks With The Ball in its Court

15. (SBU) From the beginning, the GOU told us at different levels - from Deputy PM Nemyrya downwards - that the CabMin would pass a resolution giving Tasko the necessary business once 1) OPIC and Tasko reached agreement on the modalities of the settlement, and 2) the USG and GOU signed an MOU confirming their intent to support the model to secure OPIC's swift return to Ukraine. In mid-November, OPIC and Tasko signed a protocol, and the Ambassador and Danylyshyn signed the MOU in front of the Ukrainian media. The ball then fell in the CabMin's court to pass the promised resolution.

16. (SBU) Instead, the CabMin made a very different decision. On December 3, it suddenly decided it could not give Tasko the business directly, but needed to conduct a tender to choose the company that would settle the claim. The Ministries of Economy, Defense and Industrial Policy were tasked with preparing the tender. At the Ministry of Economy, responsibility for the issue was suddenly transferred from Deputy Minister Panteyelenko to his colleague and First Deputy Minister Romanyuk. A clearly disappointed and embarrassed Panteyelenko told us he had no explanation, and referred us to Romanyuk. Equally embarrassed staffers in Nemyrya's office who had accompanied the process step-by-step also referred us to Romanyuk.

17. (SBU) Post subsequently met with Romanyuk, who told us directly that the GOU had never promised to use Tasko to settle the claim. To underscore his position he pointed out that the bilateral MOU does not mention Tasko by name, as it only refers to "a company" that will act on the GOU's behalf. He also steadfastly insisted that a tender was necessary. However, neither he nor his staffers had ever participated in the working group negotiations, where reps of almost 20 different ministries and agencies, in addition to Tasko, were present, nor had their names ever been mentioned by our previous interlocutors. Romanyuk refused to comment when told that the GOU had never mentioned a tender. Nor did he comment when told that the GOU had all along identified Tasko as the vehicle for the

settlement, that Tasko had always been at the very center of negotiations, that Tasko had reached, at the GOU's request and insistence, an understanding with OPIC, and that the GOU had expressed all this in numerous written exchanges and meetings with USG officials, including at the level of Ambassador and Deputy Prime Minister.

OPIC's Return Delayed For Months

18. (SBU) Romanyuk's assistant Oleksandr Chebanov told us on January 30 that draft instructions for the tender were being circulated within the CabMin. He refused to speculate when the tender might be announced, but said the GOU would need to give companies around four months to submit bids. The process to actually choose the company would be made thereafter. Earlier, we had been told that the GOU would ask OPIC to specify the criteria it would expect the implementing company to meet, but to date we have not received such a request. Realistically, the tender will delay OPIC's return for at least six months, if not longer. Deputy PM Nemyrya has told the Ambassador he hopes to travel to Washington in the coming weeks to sign a deal with OPIC, yet this is impossible if the GOU conducts the tender.

Why the Change in Course?

19. (SBU) Latent resistance to the proposed settlement was regularly evident in the working group negotiations. The Ministry of Justice, in particular, argued that the GOU could never take any steps that might imply, even remotely, that it was acknowledging OPIC's claim. We were told, however, that ultimately the Ministry supported the model. A source present at the December 4 CabMin meeting quoted Defense Minister Yekanurov as saying that the "whole deal stinks." Sources in Nemyrya's office later told us that the Defense Ministry had qualms about giving what it views is a sizable piece of business to Tasko, despite it being widely acknowledged that Tasko has good connections within the ministry. However, Defense Ministry officials always attended the working group meetings, and the ministry, to our knowledge, cleared all the documentation and decision memos that had been circulated in laboriously drawn-out interagency clearance processes.

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Is Tasko Still in the Game?

110. (SBU) Both Nemyrya and Yekanurov indicated in separate discussions with the Ambassador that Tasko would likely win the tender, yet neither they nor anyone else in the GOU has given assurances that this will be the case. Tasko President Pavlyukov is not at all optimistic that he will win. He said there was still opposition to the whole idea of a settlement within the GOU, and he fears that forces within the Defense Ministry and in Romanyuk's portfolio at the Economy Ministry - which has responsibility for the military/industrial complex - may actually want the business for themselves. Pavlyukov claims that a tender is not even necessary. Under Ukrainian law the GOU must execute a tender when it makes a procurement, but in this case nothing is being procured, he argues, since the GOU is giving a license to recycle and export munitions. This, he claims, is regulated by different laws and regulations, none of which contradict what the original model was intending to achieve. He also points out correctly that nobody in the GOU interagency had ever mentioned a need for a tender during the drawn-out negotiations. (Note: In August 2008 the CabMin adopted a munitions recycling program for the coming years, which did foresee that licenses would be granted via tenders. However, senior advisors to Nemyrya and Panteyelenko assured us that the program had no relevance for the envisaged OPIC solution. End note.)

Comment

111. (SBU) Various efforts to settle the OPIC claim have been undertaken in the past ten years, but never had we been so close to

an actual breakthrough. If we believe that the GOU is sincere about finding a solution, the newest permutation in the saga might only delay, but not derail, OPIC's return. However, we can no longer be certain that the GOU leadership is truly willing to take the political steps necessary for OPIC's return under the current model.

Throughout the lengthy negotiations, the GOU was careful not to commit to anything. It indicated that it would contribute its part by giving Tasko the business it needed to pay the claim, but only after Tasko and OPIC reached agreement and the USG signed the MOU. When these conditions were fulfilled, the GOU balked. We may never know precisely what is preventing Tymoshenko and Nemyrya from acting more resolutely. Both have repeatedly stated that OPIC's return is a top priority, yet their actions do not support their assertions, and Nemyrya's statement that he wants to sign a deal in Washington in the coming weeks reveals a disconnect with what his own bureaucracy is doing. When the MOU was signed, OPIC announced that it will support at least \$500 million of new U.S. investment in the first phase after its return to Ukraine. Ukraine badly needs this investment, and OPIC's rapid return would be an important sign of U.S. confidence in Ukraine's economy at a time when investors have turned their back on the country. Yet the GOU's latest actions cast doubt on its determination to take the steps necessary to remove this irritant from the bilateral relationship. End comment.

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